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UNCLAS SECTION 01 OF 02 ROME 004541

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SUBJECT: OPPOSITION PARLIAMENTARIAN PAINTS A SOMBER VIEW OF
ITALYS ECONOMY

REF: MILAN 00639

1. (SBU) SUMMARY: CENTER-LEFT PARLIAMENTARIAN NICOLA ROSSI EXPRESSED DEEP CONCERN ABOUT ITALYS ECONOMY IN A SEPTEMBER 24TH CONVERSATION WITH ECONOFFS. CIRCUMSPECT IN HIS CRITICISM OF THE CENTER-RIGHT GOVERNMENT, ROSSI ARGUED, NONETHELESS, THAT WITHOUT SIGNIFICANT STRUCTURAL REFORMS, ECONOMIC GROWTH IN ITALY WILL CONTINUE TO BE WEAK. HE CONTENDED THAT THE GAP IN ECONOMIC POTENTIAL BETWEEN THE U.S. AND EUROPE IS WIDENING AND, EVEN AMONG EUROPEAN COUNTRIES, ITALY IS FALLING FURTHER BEHIND. END SUMMARY.

2. (U) ON THE EVE OF THE BERLUSCONI GOVERNMENTS BUDGET ET PRESENTATION TO PARLIAMENT, WE MET WITH NOTED ECONOMIST AND LONG-TIME EMBASSY CONTACT NICOLA ROSSI. ROSSI WAS ELECTED TO THE LOWER CHAMBER OF PARLIAMENT IN 2002 ON A DEMOCRATICI DI SINISTRA, LULIVIO DEMOCRATS OF THE LEFT/OLIVE TREE COALITION TICKET. PRIOR TO BEING ELECTED, ROSSI WAS ECONOMIC ADVISOR TO THEN-PRIME MINISTER DALEMA; HEADED DALEMAS COUNCIL OF ECONOMIC EXPERTS; AND SERVED AS AN ADVISOR TO THEN-TREASURY MINISTER VINCENZO VISCO. ROSSI HAS HIS DOCTORATE IN ECONOMICS FROM THE LONDON SCHOOL OF ECONOMICS.

3. (U) ITALYS ECONOMIC FOUNDATION IS SHAKY, ROSSI COMMENTED. GROWTH IS STAGNANT, JUST 0.4 PERCENT, OR LESS, PROJECTED FOR 2003. ITALYS INFLATION RATE OF 2.9 PERCENT IN A TWELVE-MONTH PERIOD, JULY 2002-JULY 2003, IS ONE PERCENT HIGHER THAN THE AVERAGE FOR THE EURO-ZONE ECONOMIES. THE TREND IS VERY WORRISOME, HE DECLARED.

4. (SBU) AVOIDING OUTRIGHT PARTISAN CRITICISM OF THE BERLUSCONI ADMINISTRATION, ROSSI STATED THAT THE RULING RULING GOVERNMENT SQUANDERED AN OPPORTUNITY TO TACKLE ITALYS ECONOMIC PROBLEMS HEAD ON. COMING INTO OFFICE WITH A STRONG MAJORITY, THE GOVERNMENT HAD THE POLITICAL STRENGTH TO ADOPT REAL REFORMS. INSTEAD, HE SAID, THE GOVERNMENT HAS RELIED ON ONE-TIME MEASURES TO PROP UP THE ECONOMY AND KEEP ITALIAN FINANCES IN LINE WITH STABILITY AND GROWTH PACT DEFICIT TARGETS. ROSSI REMARKED, WRYLY, THAT EVEN WITH SUCH MEASURES, "IF THE BLANKET IS SHORT, YOUR FEET STILL GET COLD.

5. (SBU) CONTINUING, HE CONTENDED THAT THE BERLUSCONI GOVERNMENTS STRATEGY IS TO DO JUST ENOUGH TO STAY WITHIN THE STABILITY AND GROWTH PACT DEFICIT GOAL OF 3 PERCENT. TO MAKE THE BOOKS LOOK BETTER, THE GOI RECENTLY PRESENTED A BILL TO PARLIAMENT TO USE ANTICIPATED REVENUES IN 2004 FOR 2003 EXPENDITURES. ROSSI ALSO RAISED A RED FLAG ABOUT THE PRIMARY SURPLUS, A KEY BUDGETARY INDICATOR (REVENUES MINUS THE NET EXPENSE OF INTEREST PAYMENTS). THE BUDGET SURPLUS DECLINED FROM FIVE PERCENT OF GDP IN 1997 TO AN ESTIMATED D TWO PERCENT OF GDP THIS YEAR. (NOTE: THIS AGGREGATE IS CONSIDERED IMPORTANT BECAUSE PRIMARY SURPLUS FUNDS ARE USED TO PAY INTEREST ON THE PUBLIC DEBT, AND THE EU WATCHED THIS INDICATOR WAS CAREFULLY BEFORE ITALYS ADMISSION INTO THE EMU. END NOTE). ROSSI SAID THE GOVERNMENT SHOULD HAVE TAKEN ADVANTAGE OF LOW INTEREST RATES AND IMPLEMENTED MEASURES TO REDUCE THE DEBT/GDP RATIO, WHICH CONTINUES TO BE ABOVE 100 PERCENT -- WELL ABOVE THE 60 PERCENT MAASTRICHT TARGET.

6. (SBU) ROSSI DID MAKE ONE POINTED JAB AT THE RULING GOVERNMENT, BY ARGUING THAT THE BERLUSCONI GOVERNMENTS LACK OF ACTION INJECTED MASSIVE UNCERTAINTY INTO THE ECONOMIC SYSTEM AMONG FIRMS AND HOUSEHOLDS ALIKE.

7. (SBU) BROADENING HIS CRITIQUE, ROSSI COMMENTED THAT ITALIAN AND OTHER EUROPEAN LEADERS ARE NOT TACKLING THE HARD PROBLEMS THEMSELVES BUT INSTEAD ARE WAITING FOR A U.S.-LED RECOVERY TO HELP STIMULATE THEIR ECONOMIES. IN ADDITION, IT IS CLEAR THAT THE FRENCH AND GERMANS ALSO WANT ANT TO ENCOURAGE BRUSSELS TO EASE UP ON STABILITY AND GROWTH PACT RULES, HE ARGUED. HOWEVER, AN EASING OF RULES WOULD BE EXACTLY THE WRONG THING FOR ITALY. A MORE FLEXIBLE PACT WOULD LIKELY PUSH UP INTEREST RATES. ITALY, WITH A HIGHER DEBT TO GDP BURDEN THEN EITHER FRANCE OR GERMANY, COULD ILL AFFORD HIGHER INTEREST RATES. ITALY, HE SAID, SHOULD BE THE WARDEN DEFENDING THE PACT, NOT AN ADVOCATE FOR

WEAKENING IT.

18. (U) REGARDING PENSION REFORM, THE DRAFT PROPOSALS ARE
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L, WOULD REQUIRE
ITALIANS FROM 2008 ONWARDS TO PAY 40 RATHER THAN 35 YEARS
OF CONTRIBUTIONS BEFORE THEY CAN RETIRE. FURTHER DISCUSSION
OF THE PENSION REFORM MEASURES WILL BE REPORTED SEPTEL. END
NOTE.) THE PERCENTAGE OF WORKERS COVERED BY THESE NEW
MEASURES IS SMALL. IN THE SHORT TERM, SPENDING ON PENSIONS
IS EXPECTED TO INCREASE.

19. (U) ROSSI PRAISED THE GOVERNMENTS RECENT LABOR REFORM
MEASURES, WHICH WILL ENCOURAGE, FOR EXAMPLE, THE CREATION
OF PART-TIME JOBS AND JOB-SHARING. NONETHELESS, HE QUERIED
WHETHER THE RIGHT REFORMS WERE PURSUED AND ADOPTED.
ITALIAN LABOR MARKETS ARE FLEXIBLE IN TERMS OF ENTRY THE
FINDING OF A NEW JOB OR HIRING OF NEW EMPLOYEES. THE
GREATER DIFFICULTY IS IN TERMS OF EXITING - THE DISMISSAL
OF EMPLOYEES OR DOWNSIZING OF WORKFORCES, HE REMARKED.

110. (SBU) OVERALL, ROSSI IS PESSIMISTIC ABOUT THE FUTURE
PERFORMANCE OF THE ITALIAN ECONOMY. EVEN BEYOND PENSION
AND LABOR REFORMS, ITALIANS NEED TO RECAPTURE THEIR ABILITY
TO INNOVATE, HE ARGUED. WE WILL CONTINUE TO FALL BEHIND
UNLESS WE KNOW HOW TO INNOVATE AND TO BECOME ENTREPRENEURS.
EUROPE NEEDS TO CATCH UP WITH THE UNITED STATES; WE NEED TO
CATCH UP WITH EUROPE. HE ALSO URGED A FASTER PROCESS OF
LIBERALIZATION OF ENERGY AND OTHER KEY MARKETS, WHICH, HE
SAID, ITALY AS WELL AS FRANCE AND GERMANY HAVE LARGELY
STOPPED.

111. (SBU) COMMENT: THE OPPOSITION, WITH AN EYE TO THE 2004
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PARLIAMENTARY ELECTIONS, WILL USE ITALYS CONTINUED ANEMIC
ECONOMIC PERFORMANCE TO CHALLENGE THE RULING GOVERNMENT;
AND ROSSI, AS AN OPPOSITION PARLIAMENTARIAN, CLEARLY HAS A
VESTEDINTEREST IN CRITICIZING THE RULING GOVERNMENT. THAT
SAID, EVEN BERLUSCONIS SUPPORTERS ARE ECHOING MANY OF
ROSSIS COMMENTS, ALTHOUGH COALITION MEMBERS SHARE
CULPABILITY FOR NOT PURSUING MORE VIGOROUS ECONOMIC REFORM.
CONCERNED ABOUT LOSING THE SUPPORT OF THEIR ELECTORATE,
JUNIOR MEMBERS, SUCH AS THE NORTHERN LEAGUE, HAVE
DELIBERATELY THWARTED GOVERNMENT EFFORTS TO PURSUE MORE
FUNDAMENTAL PENSION REFORM (REFTEL).

112. (U) IN ADDITION, CONFINDUSTRIA, THE LARGEST EMPLOYERS
ASSOCIATION, HAS STATED THAT THE PENSION REFORM PROPOSAL IS
NEITHER BOLD NOR AGGRESSIVE ENOUGH, (ALTHOUGH CONFINDUSTRIA
IS EXPECTED TO SUPPORT THE PACKAGE IN EXCHANGE FOR LOWER
PAYROLL TAX RATES FOR SOME EMPLOYEES). CONFINDUSTRIA HAS
ALSO MADE SIMILAR COMMENTS ABOUT THE GOVERNMENTS OVERALL
ECONOMIC REFORMS. THE DEBATE OVER THE BUDGET IN THE NEXT
EXT
FEW WEEKS WILL SHOW WHETHER, ONCE AGAIN, THE STATUS QUO
WILL PREVAIL IN ITALY. END COMMENT.

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